Supreme Court, U.S.
FILED
JAN 3 1995
OFFICE OF THE CLERK

No. 94-798

In the Supreme Court of the United States

OCTOBER TERM, 1994

UNITED STATES LINES REORGANIZATION TRUST, SUCCESSOR TO UNITED STATES LINES (S.A.), INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Before it was amended in 1984, Section 546(a) of the Bankruptcy Code provided that an action to avoid a preference could not be commenced "after the earlier of—(1) two years after the appointment of a trustee under [certain sections of the Bankruptcy Code] * * * or (2) the time the case is closed or dismissed." 11 U.S.C. 546(a). The question presented is whether the two-year limitation period in subsection (a)(1) of former Section 546 applied to a preference-avoidance action brought by a debtor in possession.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statutory provision involved	2
Statement	2
Argument	5
Conclusion	8

TABLE OF AUTHORITIES

Cases:

Century Brass Prods., Inc., In re, 22 F.3d 37 (2d Cir. 1994)	5, 6, 7
Coastal Group Inc., In re, 13 F.3d 81 (3d Cir. 1994)	6, 8
Korvettes, Inc., In re, 67 B.R. 730 (S.D.N.Y. 1986)	4
Maurice Sporting Goods, Inc. v. *Maxway Corp.*, cert. denied, No. 94-632 (Nov. 28, 1994)	5
Maxway Corp., In re, 27 F.3d 980 (4th Cir. 1994), cert. denied, No. 94-632 (Nov. 28, 1994)	6
Softwaire Centre Int'l, Inc., In re, 994 F.2d 682 (9th Cir. 1993)	6
Zilkha Energy Co. v. *Leighton*, 920 F.2d 1520 (10th Cir. 1990)	6, 7-8

Statutes:

Bankruptcy Code (11 U.S.C.):	
Ch. 5:	
11 U.S.C. 502(d)	5
11 U.S.C. 546	4
11 U.S.C. 546(a)	2, 4, 5, 6
11 U.S.C. 546(a)(1)	4, 5, 6, 7
11 U.S.C. 547(b)	4, 7
Ch. 11	3, 7
11 U.S.C. 1107	7
11 U.S.C. 1107(a)	7

Statutes—Continued: Page

Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 6
§ 216, 108 Stat. 4126-4127 ..... 2, 6
§ 702(b)(1), 108 Stat. 4150 2

Miscellaneous:

S. Rep. No. 989, 95th Cong., 2d Sess. (1978) 7

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OPINION BELOW

The opinion of the court of appeals (Pet. App. A1-A8) is reported at 30 F.3d 385. The opinion of the district court (Pet. App. A13-A43) is reported at 162 B.R. 410. The opinion of the bankruptcy court (Pet. App. A46-A84) is reported at 132 B.R. 247.

JURISDICTION

The judgment of the court of appeals was entered on July 28, 1994. Pet. App. A9-A10. The petition for a writ of certiorari was filed on October 25, 1994. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY PROVISION INVOLVED

Before its amendment in 1994, Section 546(a) of the Bankruptcy Code, 11 U.S.C. 546(a), provided in relevant part:

> An action or proceeding under section 544, 545, 547, 548, or 553 of this title may not be commenced after the earlier of —
>
> (1) two years after the appointment of a trustee under [certain sections of the Bankruptcy Code] * * * or
>
> (2) the time the case is closed or dismissed.[1]

STATEMENT

1. Petitioner, United States Lines Reorganization Trust, is the successor under a confirmed bankruptcy reorganization plan to United States Lines (S.A.), Inc., a

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[1] Section 546(a) was amended effective October 22, 1994, by the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 216, 108 Stat. 4126-4127. As amended, Section 546(a) provides in relevant part:

> An action or proceeding under section 544, 545, 547, 548, or 553 of this title may not be commenced after the earlier of —
>
> (1) the later of —
>
> (A) 2 years after the entry of the order for relief; or
>
> (B) 1 year after the appointment or election of the first trustee under [certain sections of the Bankruptcy Code] * * * if such appointment or such election occurs before the expiration of the period specified in subparagraph (A); or
>
> (2) the time the case is closed or dismissed.

The parties agree that the present case is governed by the prior version of Section 546(a). See Pet. 11 & n.11.

shipping company (both of which will hereafter be referred to as "USL"). USL owned three ships on which the federal Maritime Administration (MARAD) held an undersecured mortgage. In 1986, another shipping company, Lykes Brothers Steamship Company (Lykes), offered to charter the three ships from USL. The charters were made subject to the approval of MARAD. MARAD agreed to approve the charters provided that USL assign the payments (the "charter hire") that Lykes was to make under the charters to MARAD. USL agreed to do so. Pet. App. A3, A16-A17, A49-A50.

The arrangements among USL, Lykes, and MARAD were formalized in a series of written agreements signed on November 4, 1986. Under the agreements, Lykes would pay the charter hire to an intermediary, Chemical Bank. Chemical Bank would forward the charter hire to USL as long as MARAD received no demand on its mortgage guarantees. If MARAD received such a demand, however, Chemical was, upon receiving notice of the demand, to stop forwarding the charter hire to USL pending instructions from MARAD. It is this assignment agreement between USL and MARAD that USL sought to avoid in this action. Pet. App. A3-A4, A17, A50-A52.

On November 24, 1986, USL filed a petition in the United States Bankruptcy Court for the Southern District of New York, seeking relief under Chapter 11 of the Bankruptcy Code. USL continued operating as a debtor in possession. In early 1987, MARAD received a demand on its mortgage guarantees and notified Chemical Bank to hold all further charter hire paid by Lykes. Chemical Bank did so, in accordance with the assignment agreement of November 4, 1986. At the end of the first year of the charters, MARAD agreed to an

extension of the charters and related agreements for two more years. Pet. App. A4, A17-A18, A52-A53.

In May, 1989, the bankruptcy court confirmed USL's plan of reorganization. Under the plan, USL assumed the charters. The plan did not address the status of the assignment agreement. Pet. App. A4, A19, A55.

2. Two years and ten months after USL filed for bankruptcy, USL brought this action to avoid the assignment agreement under 11 U.S.C. 547(b). Pet. App. A4. MARAD responded, among other things, that the action was untimely. USL replied that the action was timely under former 11 U.S.C. 546(a) (see page 2 and note 1, *supra*), as construed in *In re Korvettes, Inc.*, 67 B.R. 730 (S.D.N.Y. 1986). See Pet. App. A5. At that time, Section 546(a) stated that a preference-avoidance action could not be brought after the earlier of "(1) two years after the appointment of a trustee" or "(2) the time the case is closed or dismissed." 11 U.S.C. 546(a). In *Korvettes*, the district court held that the two-year limitation period in subsection (a)(1) of former Section 546 did not apply to a preference-avoidance action by a debtor in possession, because in such a case a trustee has never been appointed. 67 B.R. at 733-734; see Pet. App. A5.

The bankruptcy court granted summary judgment for USL, Pet. App. A46-A84, A85-A88, relying on *Korvettes* to reject MARAD's timeliness objection, *id.* at A59. The district court affirmed. *Id.* at A13-A43.[2]

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[2] The district court also affirmed the bankruptcy court's holdings that MARAD had waived sovereign immunity from this action and that the assignment agreement was avoidable under 11 U.S.C. 547(b). Pet. App. A21-A42. The court of appeals did not address those holdings, *id.* at A7, and they are therefore not at issue in this Court.

3. The United States Court of Appeals for the Second Circuit reversed, holding that this action is time-barred. Pet. App. A1-A8. The court observed that in *In re Century Brass Prods., Inc.*, 22 F.3d 37 (1994), it had "held for the first time * * * that the 'appointment of a trustee' in § 546(a)(1) was equivalent to the filing of a petition in debtor-in-possession cases" and thus had "overruled *Korvettes*." Pet. App. A5. On the authority of *Century Brass*," the court held in this case that USL's action was untimely because it was commenced more than two years after the filing of the bankruptcy petition. *Id.* at A7.[3]

ARGUMENT

1. Petitioner asks this Court to grant certiorari to decide whether former Section 546(a)(1) applied to preference-avoidance actions brought by debtors in possession. Pet. 9-25. This Court recently declined further review of that issue in *Maurice Sporting Goods, Inc.* v. *Maxway Corp.*, cert. denied, No. 94-632 (Nov. 28, 1994), and it should do so here. The issue is of no continuing importance in light of Congress's 1994 amendment of Section 546(a).

Before Section 546(a) was amended in 1994, the courts of appeals differed with regard to the question presented here. The Fourth Circuit had held that former Section 546(a)(1) did not apply to preference-avoidance actions brought by debtors in possession. Every other circuit to

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[3] USL argued in the court of appeals that, "even if *Century Brass* applies," 11 U.S.C. 502(d) "still prevents MARAD from reaping the alleged benefit of the assignment." Pet. App. A7. The court determined that the Section 502(d) issue had not been adequately briefed and might require further factual development. *Id.* at A8. It accordingly remanded the case to the bankruptcy court for consideration of that issue. *Ibid.*

consider the issue, however, had reached a contrary conclusion.[4]

Congress resolved the disagreement in the lower courts by amending Section 546(a) in the Bankruptcy Reform Act of 1994 (1994 Reform Act), Pub. L. No. 103-394, 108 Stat. 4106. Section 546(a)(1) now provides that preference-avoidance actions are timely if brought before the later of "(A) 2 years after the entry of the order for relief" or "(B) 1 year after the appointment or election of the first trustee * * * if such appointment or such election occurs before the expiration of" the original two-year period. 1994 Reform Act § 216, 108 Stat. 4126-4127. As amended, Section 546(a)(1) sets an absolute time limit for a preference-avoidance action that applies regardless whether the action is brought by a debtor in possession or a trustee. Thus, the issue of interpretation that arose under former Section 546(a)(1) will not arise in preference-avoidance actions brought in bankruptcy cases commenced after the effective date of the amendment, October 22, 1994. 1994 Reform Act § 702(b)(1), 108 Stat. 4150.

Despite the amendment, petitioner claims that review by this Court is warranted because of the large number of bankruptcy cases pending on the effective date of the amendment. Pet. 12. Review is not warranted on that ground, however, since it is unlikely that any more than

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[4] Compare *In re Century Brass Prods., Inc.*, 22 F.3d 37, 40 (2d Cir. 1994) (former Section 546(a)(1) applied to debtors in possession); *In re Coastal Group Inc.*, 13 F.3d 81, 84 (3d Cir. 1994) (same); *In re Softwaire Centre Int'l, Inc.*, 994 F.2d 682, 684 (9th Cir. 1993) (same), and *Zilkha Energy Co.* v. *Leighton*, 920 F.2d 1520, 1524 (10th Cir. 1990) (same) with *In re Maxway Corp.*, 27 F.3d 980, 985 (4th Cir. 1994) (former Section 546(a)(1) did not apply to debtors in possession), cert. denied, No. 94-632 (Nov. 28, 1994).

a tiny fraction of pending cases will give rise to preference-avoidance actions by debtors in possession the timeliness of which depends on resolution of the question presented here.

2. In any event, the court of appeals in this case correctly held that former Section 546(a)(1) of the Bankruptcy Code applies to preference-avoidance actions brought by debtors in possession. Pet. App. A7. That holding comports with the language and purpose of the Code.

As relevant here, former Section 546(a)(1) provided that an action to avoid a preference under Section 547(b) had to be brought within two years after appointment of a trustee. Section 547(b) in turn authorizes trustees to avoid certain pre-petition transfers. Section 547 does not, however, expressly authorize a debtor in possession to bring a preference-avoidance action. That authority is found instead in Section 1107(a). Section 1107(a) subjects a debtor in possession to "any limitations" that the Code imposes on a Chapter 11 trustee. 11 U.S.C. 1107(a); see also S. Rep. No. 989, 95th Cong., 2d Sess. 116 (1978) (Section 1107 "places a debtor in possession in the shoes of a trustee in every way"). The Second Circuit has correctly held that the two-year limitation period in former Section 546(a)(1) is one of the "limitations" to which debtors in possession are subject, and that the limitation is triggered by the filing of a bankruptcy petition, because that event is analogous to the appointment of a Chapter 11 trustee. *In re Century Brass Prods., Inc.*, 22 F.3d 37, 40 (1994).

The Second Circuit's interpretation accords with the purpose of the Code to treat Chapter 11 trustees and debtors in possession alike. "[T]here would be no reason to create a different limitation period for the filing of actions by the two fiduciaries." *Zilkha Energy Co.* v.

Leighton, 920 F.2d at 1524. Applying the former two-year limitation period to a debtor in possession "complement[ed] the [debtor in possession's] duty to negotiate in good faith with the individual creditors against whom the [debtor in possession] may have preference or avoidance claims and to disclose early on to its creditors the potential for recovery of assets for the estate." *In re Coastal Group Inc.*, 13 F.3d at 85.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JANUARY 1995